

**STATE OF IOWA
DEPARTMENT OF COMMERCE
BEFORE THE IOWA UTILITIES BOARD**

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|-------------------------------------|------------------------------------|
| IN RE: | : DOCKET NO. RPU-2016-_____ |
| | : |
| LIBERTY UTILITIES (MIDSTATES | : |
| NATURAL GAS) CORP. D/B/A | : |
| LIBERTY UTILITIES | : |

**DIRECT TESTIMONY
OF
JILL M. SCHWARTZ**

I. INTRODUCTION

1

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Jill M. Schwartz. My business address is Liberty Utilities, 2751
4 North High Street, Jackson, MO 63755.

5 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6 A. I am employed by Liberty Utilities Services Corp. as the Utility Rates and
7 Regulatory Manager for Liberty Utilities (Midstates Natural Gas) Corp. d/b/a
8 Liberty Utilities (“Liberty Midstates,” or the “Company”). I am responsible for
9 public utility rates and regulatory affairs for Liberty Midstates’ natural gas
10 operations in Illinois, Missouri and Iowa.

11 **Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND**
12 **WORK EXPERIENCE.**

13 A. I am a graduate of John E. Simon School of Business at Maryville University in
14 St. Louis, Missouri with a Bachelor of Science in Accounting.

1 From May 2001 to February 2015, I was employed by The Boeing Company in a
2 variety of accounting capacities, ensuring compliance with the Federal
3 Acquisition Regulation Mandatory Disclosure rules and developing and
4 delivering labor compliance training for all Boeing employees.

5 **Q. WHAT ARE YOUR CURRENT EMPLOYMENT RESPONSIBILITIES?**

6 A. My responsibilities consist of reviewing, preparing and assisting in regulatory
7 filings and related activities for Liberty Midstates. My responsibilities also
8 include the preparation of written testimony, exhibits, and work papers in support
9 of rate applications and other regulatory filings.

10 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE IOWA UTILITIES**
11 **BOARD (“BOARD”) OR ANY OTHER REGULATORY AGENCY?**

12 A. Yes. I have testified before the Illinois Commerce Commission.

13 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY IN THIS**
14 **PROCEEDING?**

15 A. The purpose of my Direct Testimony is to provide, and explain the basis for, the
16 Company’s Iowa revenue requirement.

17 **Q. ARE YOU SPONSORING ANY EXHIBITS WITH YOUR TESTIMONY?**

18 A. Yes. I am sponsoring Schwartz Direct Exhibit JMS-1: Liberty Midstates’ Overall
19 Revenue Requirement; Schwartz Direct Exhibit JMS-2: Liberty Midstates Test
20 Year Rate Base, Schwartz Direct Exhibit JMS-3: Liberty Midstates Test Year
21 Statement of Operating Income; and Schwartz Direct Exhibit JMS-4: Overall Cost
22 of Capital.

1 **Q. WAS THE INFORMATION CONTAINED IN YOUR EXHIBITS**
2 **OBTAINED OR DERIVED FROM THE BOOKS AND RECORDS OF**
3 **THE COMPANY?**

4 A. Yes, the information contained in my exhibits were obtained or derived from the
5 books and records of Liberty Midstates for the twelve months ended December
6 31, 2015.

7 **I. REVENUE REQUIREMENT**

8 **Q. WHAT IS MEANT BY THE TERM “REVENUE REQUIREMENT”?**

9 A. A utility’s “revenue requirement” is the sum of its operations and maintenance
10 (“O&M”) expenses, depreciation expense, income and other taxes and a fair
11 return on the utility’s rate base. The revenue requirement is determined based on
12 utility revenue and expenses in a “test year.” In Iowa, as I understand it, pro
13 forma adjustments are permitted to recognize known and measurable changes to
14 test year revenue and expenses that will occur within twelve months of the date
15 the rate case is filed (the “pro forma period”). When the revenue requirement
16 exceeds the utility’s test year revenues, a revenue deficiency exists, and a rate
17 increase is needed.

18 **Q. WHAT TEST YEAR IS LIBERTY MIDSTATES PROPOSING IN THIS**
19 **CASE?**

20 A. Liberty Midstates is proposing use of the calendar year ended December 31, 2015
21 as the historic test year, updated for known and measurable changes through June
22 30, 2016.

1 Q. BASED ON LIBERTY'S TEST YEAR REVENUES, IS THE COMPANY
2 ABLE TO EARN A FAIR RETURN ON ITS INVESTMENTS?

3 A. No. Based on the Liberty Midstates' test year rate base, revenues and expenses,
4 the Company's current rate of return is -1.06%.

5 Q. WHAT IS THE REVENUE REQUIREMENT FOR LIBERTY
6 MIDSTATES' IOWA GAS OPERATIONS?

7 A. Liberty Midstates has an overall revenue requirement for its Iowa gas operations
8 of \$3,176,268 and a current revenue deficiency of \$1,057,139.

9 Q. WHAT IS THE PRO FORMA PERIOD?

10 A. The pro forma period is the twelve months ended July 25, 2017.

11 Q. PLEASE DESCRIBE SCHWARTZ DIRECT EXHIBIT JMS-1.

12 A. Schwartz Direct Exhibit JMS-1 presents the Company's proposed revenue
13 requirement and the overall revenue requirement calculation. Schwartz Direct
14 Exhibit JMS-2 shows the test year 2015 rate base along with pro forma
15 adjustments and the resulting pro forma rate base. Schwartz Direct Exhibit
16 JMS-3 shows the test year 2015 statement of operating income with pro forma
17 adjustments and the resulting pro forma operating income. Schwartz Direct
18 Exhibit JMS-4 shows the overall cost of capital used in the calculation of the
19 revenue requirement.

20 II. RATE BASE

21 **Q. WHAT IS THE COMPANY'S PRO FORMA RATE BASE?**

1 A. As shown on Schwartz Direct Exhibit JMS-2, the Company's pro forma rate base
2 is \$6,531,685. It is comprised of the 13 month average test period rate base of
3 \$5,349,226, with pro forma adjustments totaling \$1,182,459.

4 **Q. PLEASE SUMMARIZE THE COMPONENTS OF THE RATE BASE**
5 **CALCULATION SHOWN ON SCHWARTZ DIRECT EXHIBIT JMS- 2.**

6 A. Rate Base is comprised of the following key components:

- 7 (i) Net Utility Plant: gross Utility Plant in Service ("UPIS") less the reserves
8 for Accumulated Depreciation/Amortization;
9 (ii) Cash Working Capital;
10 (iii) Materials and Supplies; and,
11 (iv) Prepayments.

12 Rate Base was reduced by the following customer-contributed capital
13 components:

- 14 (v) Reserve for Bad Debt; and,
15 (vi) Accumulated Deferred Income Taxes associated with excess tax over
16 book depreciation.

17 The detail underlying each component of the rate base calculation is contained in
18 the workpapers filed in this case.

19 **Q. WHAT AMOUNT OF UPIS HAS LIBERTY MIDSTATES' INCLUDED IN**
20 **ITS TEST YEAR RATE BASE?**

21 A. As shown on Schwartz Direct Exhibit JMS-2, Line 1, the UPIS included in the
22 rate base is \$17,211,971, based on a thirteen-month average of gross plant

1 balances as of December 31, 2015 and pro forma adjustments to recover known
2 and measurable changes to plant in service through the pro forma period.

3 **Q. WHAT PRO FORMA ADJUSTMENTS WERE MADE TO UPIS?**

4 A. The Company proposes one pro forma adjustment to UPIS -- the addition of
5 \$1,400,000 to recognize Liberty Midstates' investment in the upgrade of the
6 Keokuk Gate Stations (the "Gate Stations" or the "Gate Station Project"). The
7 Gate Stations will be in service by the third quarter of 2016.

8 **Q. PLEASE DESCRIBE THE GATE STATION PROJECT.**

9 A. A gate station, in the context of a gas distribution system, reduces the pressure in
10 the line from transmission levels to distribution levels. Liberty Midstates is
11 upgrading two of its gate stations in Keokuk. One, located on Plank Road (the
12 "Plank Road Gate Station"), was placed in service in the 1950s and is situated in a
13 highly concentrated residential and commercial area ("HCA") within the city
14 limits of Keokuk. Currently the pressure coming into the station is 900 psi.

15 Over the past several years, Liberty Midstates has incurred significant
16 expense associated with digs in the HCA area in which the Plank Road Gate
17 Station is situated and also in maintenance of an in-line heater installed in the
18 1960s. Replacement parts for the in-line heater are difficult to find and
19 sometimes impossible to get. Accordingly, Liberty Midstates decided to reduce
20 the line pressure at the Airport Road Gate Station from 900 psi to 300 psi, which
21 takes the transmission line rating down to a distribution line into town. Thus
22 eliminating associated HCA's and required future digs. The Gate Station Project

1 will not require any significant pipeline construction or reconstruction and will
2 significantly increase the safety in residential and commercial areas.

3 **Q. DO YOU BELIEVE THAT THE GATE STATION PROJECT IS**
4 **PRUDENT AND THAT THE PRO FORMA ADJUSTMENT ASSOCIATED**
5 **WITH THE PROJECT IS REASONABLE?**

6 A. Yes. As discussed above, the Gate Station Project was necessary to ensure safe,
7 adequate and reliable gas service to Liberty Midstates' customers in Iowa.

8 **Q. WILL THE GATE STATION BE IN SERVICE AND USED AND USEFUL**
9 **TO LIBERTY MIDSTATES WITHIN THE PRO FORMA PERIOD?**

10 A. Yes. I reasonably expect that Liberty Midstates the Gate Station will be in service
11 and used and useful in the third quarter of 2016.

12 **Q. WHAT IS THE COST OF THE GATE STATION PROJECT?**

13 A. As stated in the Direct Testimony of Michael D. Beatty, President of Liberty
14 Midstates, the expected cost of the Gate Station Project is between \$1.4 million
15 and \$1.7 million. The Company received multiple bids for outside services
16 related to the Gate Station Project to ensure that such cost is reasonable in amount
17 and prudently incurred. In an effort to be conservative, the Company has included
18 a pro forma adjustment to UPIS for \$1.4 million for the Gate Station Project. See
19 Schwartz Direct Exhibit JMS-2, Schedule 1, Line 1. I will update my Direct
20 Testimony as the Gate Station Project progresses to keep the Board informed of
21 the status of the project and the total dollars associated with it.

22 **Q. PLEASE DESCRIBE CASH WORKING CAPITAL AND THE**
23 **ADJUSTMENT YOU HAVE MADE TO RECOGNIZE IT IN RATE BASE?**

1 A. Cash Working Capital represents the amount of investor-supplied capital, over
2 and above the investment in utility plant, needed for a utility to pay its daily
3 operating expenses necessary to provide service until the revenues from that
4 service are received. Cash working capital is included in rate base to compensate
5 investors for the use of these funds.

6 The amount of cash working capital included in rate base is usually
7 determined through a lead-lag study. A lead-lag study computes the number of
8 days between when revenues for utility services rendered are received (i.e., the
9 “revenue lag”) and the number of days between when the costs of providing
10 services are incurred and when those costs are paid by the utility to its vendors
11 (i.e., the “expense lead”). The number of days so calculated times the average
12 daily operating expenses produces the cash working capital required for
13 operations.

14 Lead-lag studies are expensive and time-consuming to perform.
15 Accordingly, on March 1, 2016 Liberty Midstates filed a “Request for Waiver”
16 pursuant to 199 IAC 1.3, asking the Board to waive the Board’s requirement for
17 Liberty Midstates to submit a recent lead-lag study. The Request for Waiver
18 (WRU-2016-0006-0222) was approved on March 25, 2016. In its order, the
19 Board determined it was reasonable for Liberty Midstates to employ the expense
20 lead and revenue lag factors derived in a recent Black Hills rate case (RPU-2010-
21 0002) as a proxy for the factors that would have been determined through a lead-
22 lag study conducted specifically for Liberty Midstates.

1 The amount of cash working capital required by Liberty Midstates as a
2 result of the methodology authorized by the Board in the Black Hills rate case is
3 \$30,138, as shown on Schwartz Direct Exhibit JMS- 2, Line 10. The detail is set
4 forth in the Company's work papers filed in this case.

5 **Q. PLEASE DESCRIBE THE ALLOCATION OF SHARED SERVICE**
6 **ASSETS INCLUDED IN RATE BASE.**

7 A. Shared Services assets are assets associated with Liberty Midstates' headquarters
8 in Jackson, Missouri that provide a benefit to all of the jurisdictional operations of
9 Liberty Midstates (i.e., Iowa, Illinois, and Missouri). These assets include an
10 Iowa allocation for the divisional headquarters building and land located in
11 Jackson, Missouri, computer hardware and software, and shared vehicles and
12 equipment. Additionally, the Shared Services assets include an Iowa allocation
13 for Liberty Midstates' parent company's corporate headquarters building and land
14 ("Davis Road") located in Oakville, Ontario, and the corporate human resources
15 information system ("HRIS").

16 **Q. WHY ARE SHARED SERVICE ASSETS INCLUDED IN RATE BASE?**

17 A. The above items are used by Liberty Midstates staff and Liberty Midstates' parent
18 company's staff to perform services in support of Liberty Midstates' Iowa
19 operations. For example, Liberty Midstates vehicles are used to transport
20 personnel to Missouri, Illinois, and Iowa locations. Therefore, we have allocated
21 the assets associated with the shared services proportionally to each jurisdiction.
22 Shared assets are allocated from Liberty Midstates to Iowa based on four factors
23 comprised of utility plant, number of customers, labor costs, and expenses.

1 **Q. PLEASE DESCRIBE THE PREPAID EXPENSES ADJUSTMENT TO**
2 **RATE BASE SHOWN ON LINE 9 OF SCHWARTZ DIRECT EXHIBIT**
3 **JMS-2.**

4 A. The pro forma adjustment for Prepaid Expenses represents the thirteen-month
5 average of payments made by the Company for various expenses including AGA
6 and SGA dues, Energy Intelligence, insurance, and systems maintenance as of
7 December 31, 2015. The prepaid expenses are shown on Schwartz Direct Exhibit
8 JMS-1, Schedule 2, Line 9, and total \$21,982.

9 **Q. PLEASE EXPLAIN HOW THE ACCUMULATED DEFERRED INCOME**
10 **TAXES SHOWN ON SCHWARTZ DIRECT EXHIBIT JMS-2, LINE 4**
11 **WERE DETERMINED.**

12 A. Liberty Midstates tracks deferred tax assets and liabilities by the temporary
13 difference between book basis and tax basis that gave rise to the deferred tax asset
14 or liability. Accumulated Deferred Income Taxes are deducted from rate base
15 based on a thirteen-month average as of December 31, 2015.

16 **III. OPERATING INCOME**

17 **A. OPERATING REVENUES**

18 Q. HAVE YOU MADE ANY ADJUSTMENTS TO THE COMPANY'S
19 OPERATING REVENUES?

20 A. Yes. As seen on Schwartz Direct Exhibit JMS-3, Schedule 1, Line 1, we have
21 included an adjustment to reduce revenues to recognize the closing of Keokuk
22 Steel Castings, a Liberty Midstates transportation customer, and to normalize
23 revenues for weather.

1 **Q. PLEASE EXPLAIN THE KEOKUK STEEL ADJUSTMENT TO**
2 **REVENUES.**

3 A. Keokuk Steel Castings was a Liberty Midstates transportation customer during the
4 test year ended December 31, 2015. In March 2016, Keokuk Steel Castings
5 closed its operations in Liberty Midstates' service territory. The pro forma
6 adjustment to recognize the loss of revenues from Keokuk Steel Castings --
7 \$X.XX -- represents twelve months of actual revenues received from this
8 customer during the period December 2014 through November 2015.

9 **Q. PLEASE EXPLAIN THE WEATHER NORMALIZATION ADJUSTMENT**
10 **TO REVENUES.**

11 A. As approved by the Board's March 25, 2016 order granting Liberty Midstates'
12 waiver request in Docket WRU-2016-0006-0222, we have included a pro forma
13 adjustment to revenues to reflect normal weather and consumption based on
14 Liberty Midstates' most recent weather normalization filing, Docket No. PGA-
15 2015-0032. The weather normalization adjustment included on Schwartz Direct
16 Exhibit JMS-3, Schedule 1, Line 1 represents an increase in revenues of \$41,707.

17 **B. Operating Expenses**

18 **Q. HAVE YOU MADE ANY ADJUSTMENTS TO THE COMPANY'S**
19 **OPERATING EXPENSES?**

20 A. Yes. As seen on Schwartz Direct Exhibit JMS-3, Schedule 1, we have included
21 several pro forma adjustments to test period operating expenses for depreciation,
22 federal and state income tax, new employees, wage increases, and rate case
23 expense.

1 **Q. PLEASE EXPLAIN THE ADJUSTMENTS TO DEPRECIATION**
2 **EXPENSE.**

3 A. The Company contracted with Alliance Consulting to conduct a depreciation
4 study. The details of the study are addressed by Liberty Midstates' witness, Mr.
5 Dane Watson. The impact of the depreciation study amounted to a total expense
6 adjustment of \$27,601, as shown on Schwartz Direct Exhibit JMS-3, Line 9.
7 Additionally, as reflected in Schwartz Direct Exhibit JMS- 3, Line 9, we have also
8 included an adjustment to depreciation expense for the pro forma rate base
9 adjustments related to the Gate Station Project and the Liberty Midstates' parent
10 company shared assets.

11 **Q. PLEASE DESCRIBE THE DERIVATION OF YOUR ADJUSTMENTS**
12 **FOR STATE AND FEDERAL INCOME TAX EXPENSE.**

13 A. The amounts of state and federal income tax expense included in the revenue
14 requirement are calculated by applying statutory state and federal income tax rates
15 to operating income before taxes. Test year income tax expense is shown on
16 Schwartz Direct Exhibit JMS- 3, Lines 14 and 15, and totals \$257,442.

17 **Q. PLEASE EXPLAIN THE EXPENSE ADJUSTMENT FOR NEW**
18 **EMPLOYEES.**

19 A. In order to continue providing safe and reliable service to Liberty Midstates
20 customers in Iowa and to mitigate an aging workforce, the Company has added
21 two additional employees. Typically operators require two to three years of
22 training and on the job experience in order to possess the skill sets required to
23 successfully perform job tasks independently. Given that the average age of the

1 Company's current operations workforce in Iowa is near retirement age, the
2 Company has hired two employees in Iowa, a construction operator and a service
3 technician, to ensure sufficient time for training the new employees and
4 facilitating the sharing and transfer of knowledge from existing employees to the
5 new employees. The cost of these new employees, which includes an estimate for
6 wages and benefits, is shown as pro forma expense adjustment on Schwartz
7 Direct Exhibit JMS-3, Schedule 1, Line 4, and totals \$105,300.

8 **Q. PLEASE EXPLAIN THE EXPENSE ADJUSTMENT FOR WAGE**
9 **INCREASES.**

10 **A.** The pro forma adjustment included on Schwartz Direct Exhibit JMS-3, Schedule
11 1, Line 8 includes a 2.5 percent increase in employee wages, totaling \$6,885 of
12 additional Administrative and General expenses.

13 **Q. PLEASE EXPLAIN THE EXPENSE ADJUSTMENT FOR CORPORATE**
14 **ALLOCATIONS.**

15 **A.** The pro forma adjustment included on Schwartz Direct Exhibit JMS-3, Schedule
16 1, Line 8 represents a 1 percent reduction in corporate allocations from Liberty
17 Midstates' parent company as a result of the January 2016 acquisition of Park
18 Water in California.

19 **Q. PLEASE DESCRIBE THE ADJUSTMENT LIBERTY MIDSTATES**
20 **MAKES FOR THE PGA ON SCHWARTZ DIRECT EXHIBIT JMS-3,**
21 **SCHEDULE 1, LINES 1 AND 2.**

22 **A.** The PGA gas charge recovers the costs of the natural gas the Company purchases
23 from its suppliers and delivers to its customers. These gas commodity revenues

1 and expenses are the subject of the PGA and its associated reconciliation
2 proceedings, and are outside the scope of this base rate proceeding. Therefore,
3 the adjustment eliminates both the revenues and expenses collected through the
4 PGA. This adjustment is shown on Schwartz Direct Exhibit JMS-3, Schedule 1
5 Lines 1 and 2.

6 **Q. PLEASE DESCRIBE THE PROPOSED PRO FORMA ADJUSTMENT**
7 **FOR RATE CASE EXPENSE INCLUDED ON SCHWARTZ DIRECT**
8 **EXHIBIT JMS-3, SCHEDULE 1, LINE 8.**

9 A. Liberty Midstates estimates that it will spend \$375,000 to prepare, file and litigate
10 this proceeding. Liberty is also required by Iowa law to pay the expenses that the
11 Board and the Office of Consumer Advocate (“OCA”) incur in this case. Liberty
12 Midstates estimates that the Board and OCA expenses will total \$225,000. The
13 Company believes it will file its next rate case not sooner than five years from
14 now. Liberty thus proposes to amortize the total rate case expense over five
15 years. Accordingly, Liberty Midstates has included an adjustment to Operating
16 Expense of \$120,000. Of course, Liberty Midstates may recover only the *actual*
17 rate case expense incurred, so the Board’s final order in this case should allow for
18 the recovery of actual rate case expense, as determined through the appropriate
19 filings following briefing of the case.

20 **IV. CONCLUSION**

21 **Q. HAS LIBERTY MIDSTATES FILED TARIFFS WITH THIS RATE CASE?**

22 A. Yes, new draft Iowa tariffs have been filed with Liberty Midstates’ rate case
23 filing.

1 **Q. HAS LIBERTY MIDSTATES PROVIDED ITS CUSTOMERS WITH**
2 **NOTICE OF THIS RATE CASE PROCEEDING.**

3 A. Yes. Prior to filing this Application, Liberty Midstates mailed to all its customers
4 a Notice of Rate Increase. The notice sent to customers was approved by the
5 Board in an order issued on July 21, 2016 in Docket No. RN-2016-0001. A copy
6 of the customer notice is attached hereto as Schwartz Direct Exhibit JMS-5.

7 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

8 A. Yes.

AFFIDAVIT

STATE OF IOWA)
) ss:
COUNTY OF POLK COUNTY)

I, Jill Schwartz, being first duly sworn on oath, do hereby depose and state:

1. I am the Utility Rates and Regulatory Manager and my business address is 275 N. High Street, Jackson, MO 63755.
2. The foregoing written Direct Testimony and exhibits thereto were prepared by me or under my direct supervision and I have directed that my written Direct Testimony to be filed with the Iowa Utilities Board on July 25, 2016.
3. I hereby affirm that my written Direct Testimony is true and correct to the best of my knowledge and belief as of the date of this affidavit.

Done at Jackson, Missouri, on July 22, 2016.

/s/ Jill Schwartz

Jill Schwartz, Utility Rates and Regulatory Manage

Subscribed and sworn to before me on July 22, 2016.

/s/ Christina Holte

Notary Public in and for said County and State of
Iowa

Commission # 766525

My commission expires February 1, 2017